

Market Attractiveness: What Marketers Look for in a New Residential Market

Illinois Commerce Commission
Electric Policy Committee Meeting
Monday, October 2, 2006



Mr. Badar Khan
Senior Vice President



Mr. Thomas Butler
Director, Business
Development



Mr. Richard Ravthon
Vice President

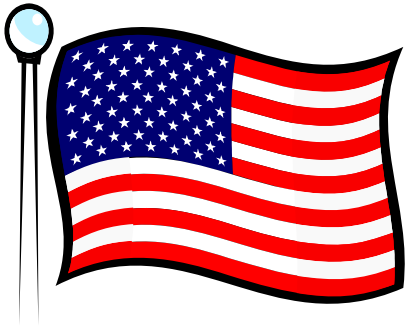
Direct Energy's Perspective

Part of Centrica, plc

- 8th largest utility in the world
- \$33 billion dollar company
- Leading provider of energy and other essential services
- More than 34 million customer relationships worldwide



Direct Energy's Perspective

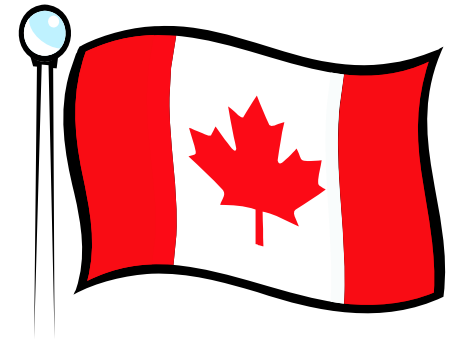


One of the largest competitive retailers
in North America.

Over 5 million customer relationships.

Over 300,000 U.S gas supply customers.

Over 900,000 U.S. electricity customers.





**Alternative Gas Supplier Certificate
(March, 2005)**

**Alternative Retail Electric Supplier Certificate
(December, 2005).**

**Actively exploring opportunities to enhance the
environment for residential electric competition
in Illinois and other states.**



Residential and Business Customers

Serving approximately 1.9 million electricity customers in Texas, we provide electricity for residences and businesses offering friendly service and reliability from a company you can trust.

Commercial-Industrial Customers

Reliant Energy Solutions provides competitive retail electricity supply to large commercial, industrial and institutional customers over 1MW in Texas, New Jersey and Maryland, supported by its unique combination of knowledge, innovation, service and reliability.

Power Generation and Supply

Our power generation and supply operations include a portfolio of strategic electric generation assets totaling approximately 16,000 megawatts in operation, under construction or under contract across the U.S

Dominion Retail, Inc.

- Started operating in 1996
- 800,000 natural gas and electricity customers; \$1.2 billion in Revenue; 80 employees
- Focus on Small Commercial and Residential Customers
- Serve Customers in 8 states (IL, OH, PA, NY, MD, CT, MA, ME)
- Operate on own Call Center, Billing Services, Energy Procurement Groups, etc.
- Serve 65,000 natural gas customers in Illinois



Five Questions Marketers Ask Before Entering a New Market

- 1. Does the structure of the utility's default rate provide alternative suppliers with a reasonable opportunity to compete?**
- 2. Will we have to create a new billing system or can we pay the utility to bill for us?**
- 3. Will we be on equal footing with utility default service in terms of uncollectible expense and mechanisms to assure payment?**
- 4. Is the process for switching energy providers simple, straightforward and efficient?**
- 5. Is there an active and ongoing effort by regulators and other policy makers to foster the development of retail competition in the market?**



Does the structure of the utility's default rate provide alternative suppliers with a reasonable opportunity to compete?

Question #1: Does the structure of the utility's default rate provide alternative suppliers with a reasonable opportunity to compete?

Answer: No

- Fundamental changes in default service design must be undertaken in order for residential customers to receive the benefit of retail competition
- Competitive retail suppliers will not enter a market where barriers to competition exist

Overview: Benefits of Retail Competition

- Competitive market forces:
 - Are more effective than economic regulation in establishing products and pricing
 - Provide each customer options to meet their individual needs (e.g., term, pricing level, price certainty)
 - Ensure that customers have a real choice of providers
 - Establish prices that facilitate efficient consumption decisions

Overview: Policy Considerations in Promoting a Competitive Market Structure

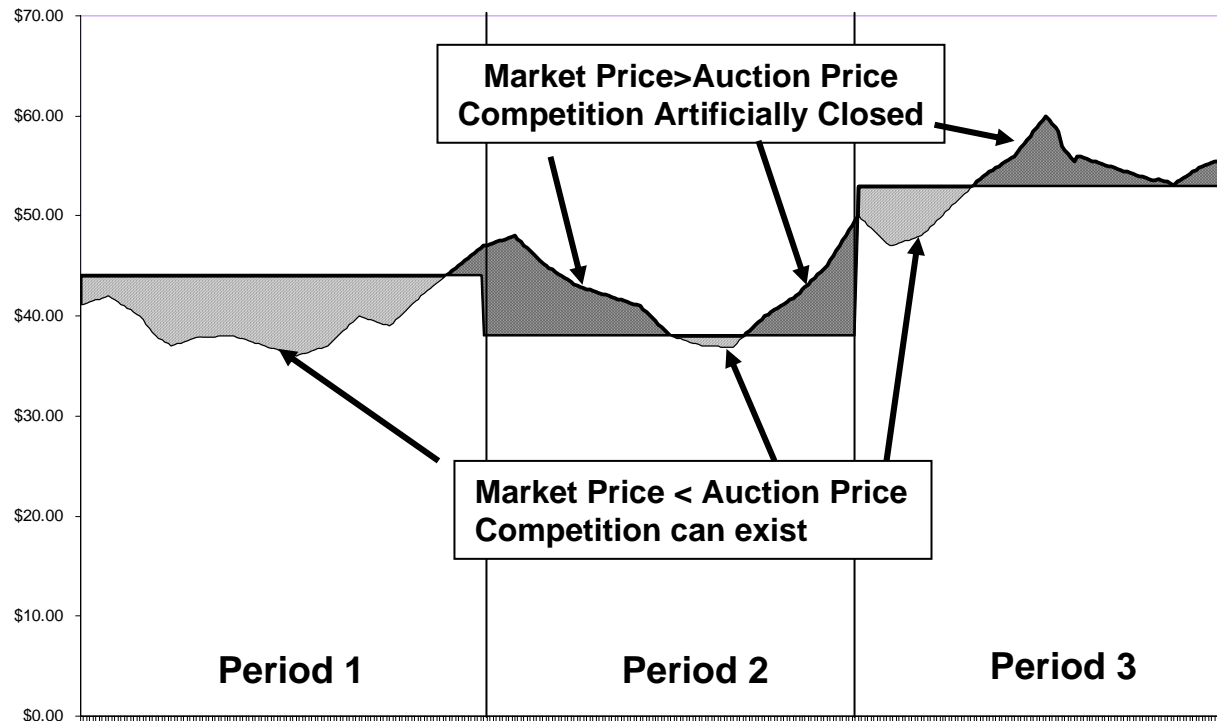
- Price “stability”
- Product innovation
- Level of marketer participation/interest
- Market oversight
- Consumer protection
- Affiliate rules – Codes of Conduct

Overview: Why the Current Default Structure Fails to Meet Consumer Needs

- The Current default structure for residential and small Commercial customers will not provide competitive retailers a reasonable opportunity to compete on a sustainable basis
 - The default structure prevents competitive retail suppliers from entering this segment of the market
 - IL consumers will not achieve benefits of competition including choice, competitive pricing, and product innovations
 - IL and the region will not have the opportunity to achieve environmental benefits resulting from reduced or shifted consumption

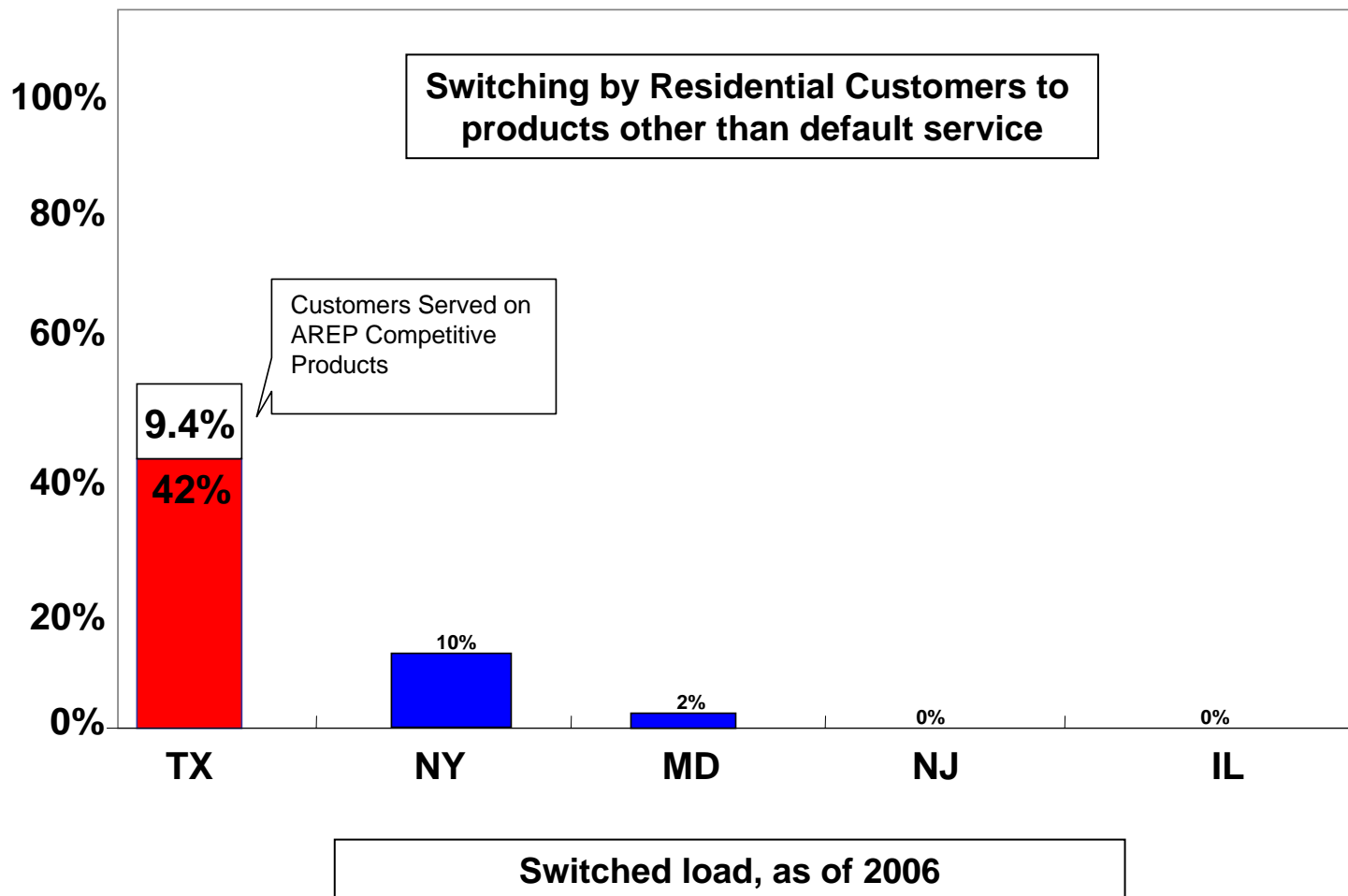
Current default structure will not allow competitive retail suppliers to enter this segment of the market

A default structure is critical in an appropriately structured competitive retail market

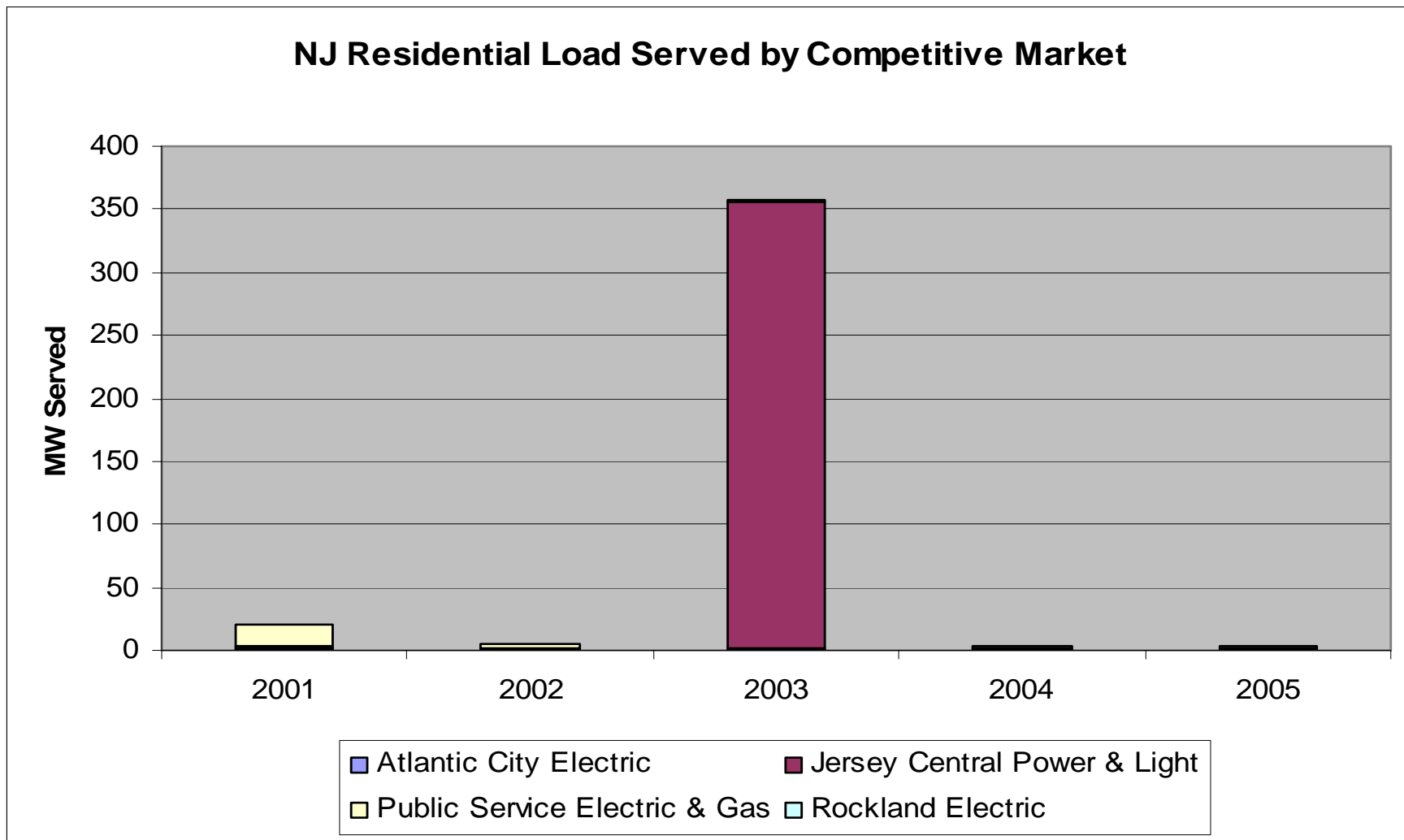


Potential for divergence of current market prices from prices established under non-market responsive, long-term contracts will prevent new entrants from entering the market.

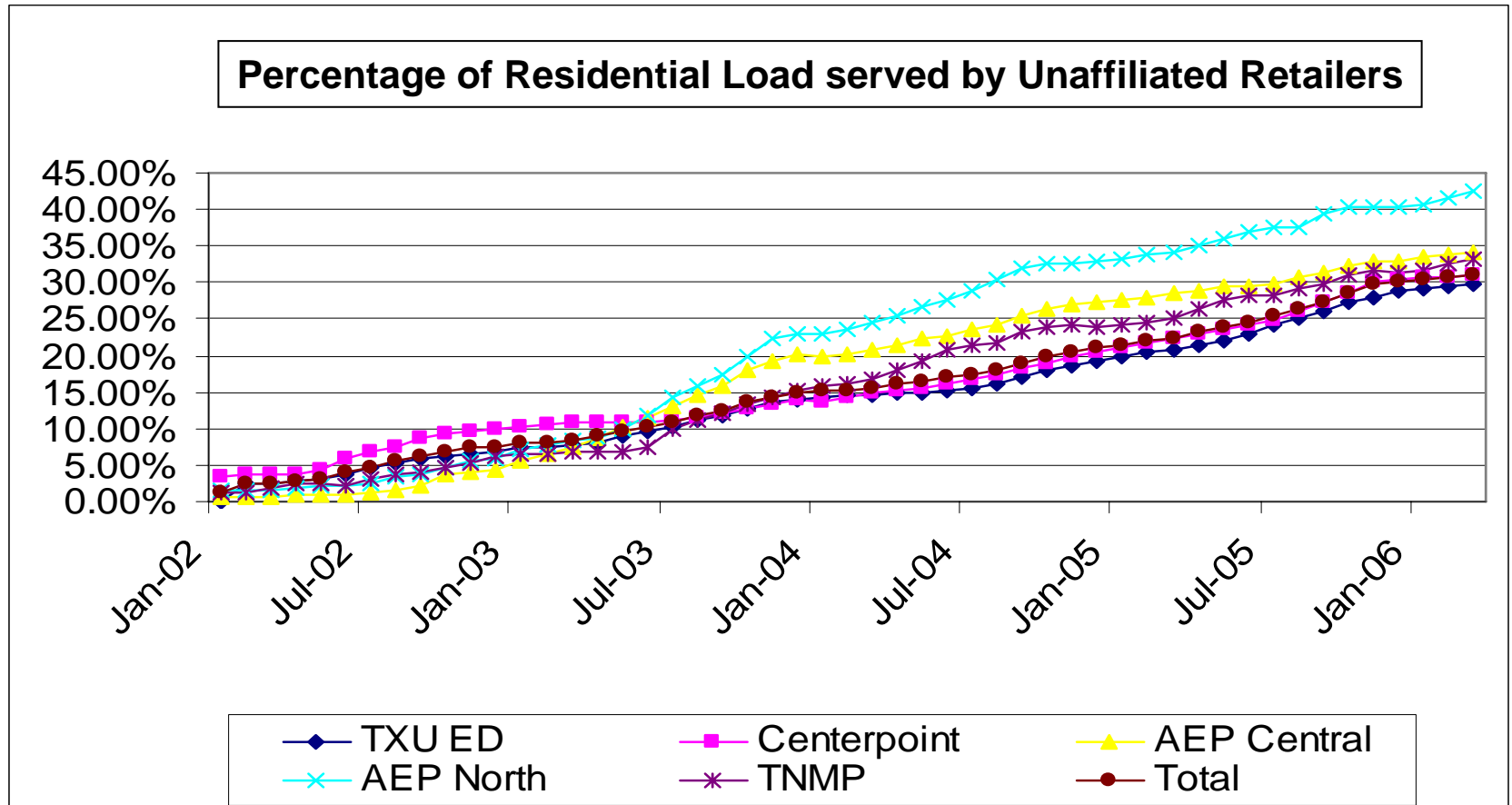
Success of Other Competitive Market Structures (as measured by Customer Switching)



Other Competitive Market Structures – a closer look at New Jersey

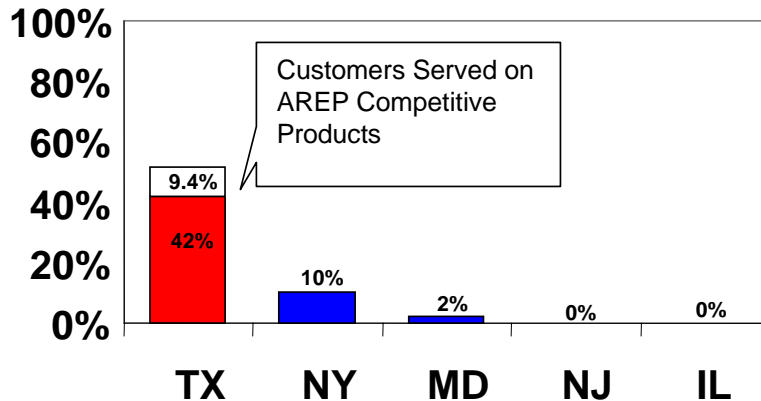


Other Competitive Market Structures -- a closer look at Texas

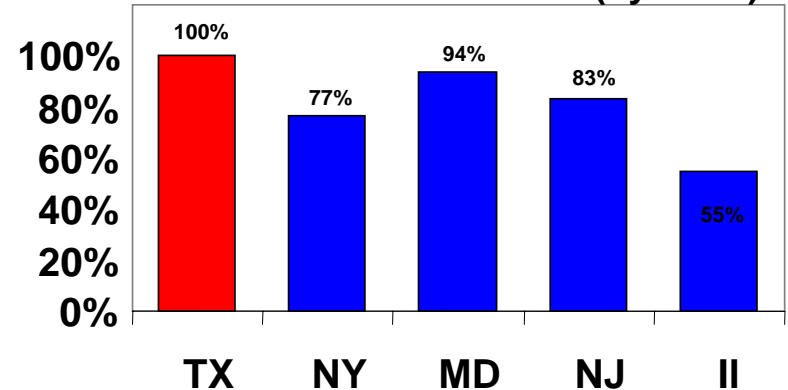


Success of Other Competitive Market Structures, Including Non-residential and Other Analogous Markets

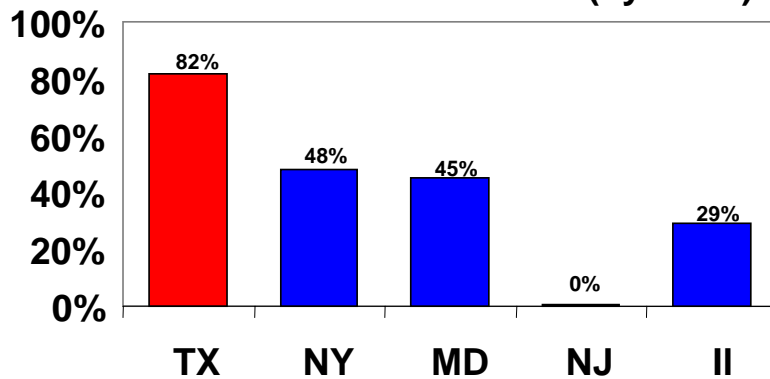
2006 Residential Switching to Non-Default Products (by Load)



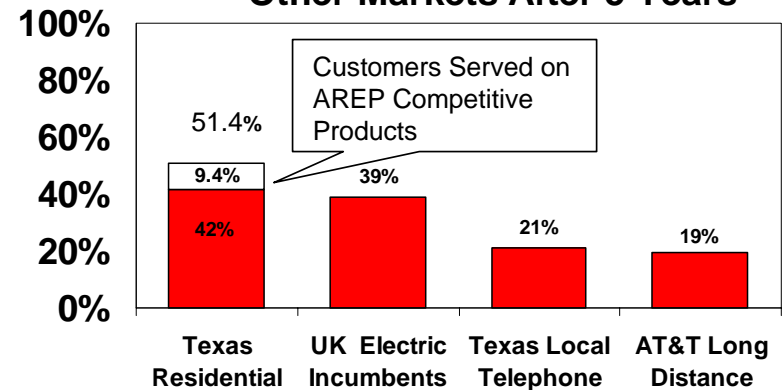
2006 Large C&I Switching to Non-Default Products (by Load)



2006 Small Commercial Switching to Non-Default Products (by Load)



Better Switching Than Other Markets After 5 Years



Sources:

Texas- Retail Transaction Reports as of (7/31/06)
<http://www.ercot.com/mktinfo/retail/index.html>

New York- NYS Electric Retail Access Migration Reports (7/31/06)
http://www.dps.state.ny.us/Electric_RA_Migration.htm

Maryland- Electric Choice Enrollment Monthly Report as of (7/31/06)
<http://www.psc.state.md.us/psc/electric/enrollmentrpt.htm>

New Jersey- Electric Statistics as of (7/31/06)
<http://www.state.nj.us/bpu/energy/elecSwitchData.shtml>
<http://www.state.nj.us/bpu/wwwroot/energy/CIEP.pdf>

Illinois- Electric Shopping Statistics as of (06/30/06)
<http://www.icc.illinois.gov/en/switchstats.aspx>

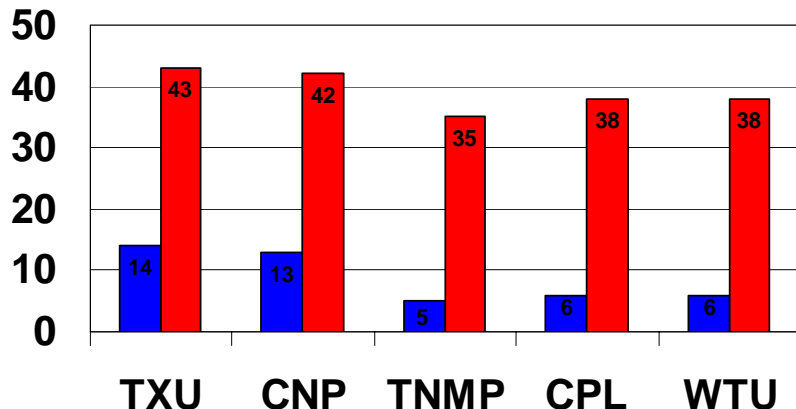
PUC-Texas- 2005 Report on Scope of Competition in Telecommunications Markets in Texas

Current Market Structure Denies Consumers the Benefits of Competition

- These benefits include:
 - Product innovation (renewable, wind-only, 1, 2, 5 year fixed prices, summer rebates, etc.)
 - Choice of varied competitors
 - Choice of products
 - Price competition and resulting economic efficiencies

Success in Other Markets – TX Residential Customers Benefit from a Vibrant Market with A Myriad Of Choices

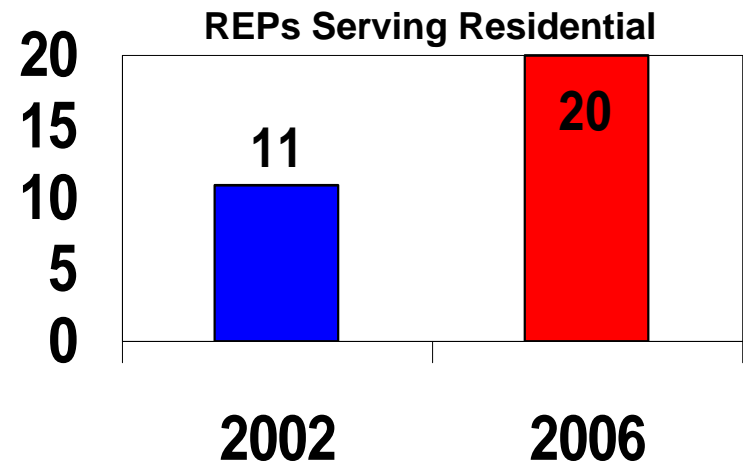
2002 vs. 2006 REP Residential Products



- ERCOT Residential Customers represent a huge market with over 5.3 Million Households.
- ERCOT Residential Customers use 20 GW of Load or about 1/3rd of all electricity in ERCOT

Residential Products Include:

- 100% Renewable
- Guaranteed Savings
- Flex Plans
- Fixed Price
- Variable Term Lengths
- Long Term Price Security-
5 Year term product available



Sources:






1- Power to Choose <http://www.powertochoose.org/> visited 9/11/06

2- US Census Bureau <http://quickfacts.census.gov/qfd/states/48000.html>


3- ERCOT http://www.ercot.com/mktinfo/retail/kd/Number_Premises_Switched_EOM_2006_07.ppt

Competitive Offers in Texas

Below is an example of the website that customers can go to for offer comparisons at: www.powertochoose.org (for zip code 77002 – Houston, on 9/29/06, 1000 kWh usage)

Electricity		Cost Per Month	Save First Year	Min. Term (Mo.)	Environ. Info	Facts Label and Terms	Average Price per kWh (1000 kWh)
Sign Up	Provider Offer						
							
	YOUR AFFILIATE REP IS: Reliant Energy Price to Beat	\$163	0	1		This is the basis for comparison.	\$0.163/kWh
Choose	First Choice Power, Inc. Simply Better Renewable	\$154	6%	12		Terms of Service ; Facts Label	\$0.154/kWh
Choose	First Choice Power, Inc. Simply Better Plan	\$137	16%	12		Terms of Service ; Facts Label	\$0.137/kWh
Choose	Amigo Energy Truly Fixed Price 12-mo Commitment Program	\$144	12%	12		Terms of Service ; Facts Label	\$0.144/kWh
Choose	Amigo Energy Truly Fixed Price 6-mo Commitment Program	\$129	21%	6		Terms of Service ; Facts Label	\$0.129/kWh
Choose	Commerce Energy Residential Variable Product	\$158	3%	1		Terms of Service ; Facts Label	\$0.158/kWh
Choose	Commerce Energy Residential Price Stopper	\$127	22%	12		Terms of Service ; Facts Label	\$0.127/kWh
Choose	Ambit Energy, LP. Residential Electric Offer	\$146	10%	1		Terms of Service ; Facts Label	\$0.146/kWh
Choose	Gexa Energy Gexa Green - 100% Pollution Free	\$161	1%	0		Terms of Service ; Facts Label	\$0.161/kWh
Choose	Gexa Energy Gexa Guaranteed	\$148	9%	12		Terms of Service ; Facts Label	\$0.148/kWh
Choose	Gexa Energy Power Plan	\$143	12%	0		Terms of Service ; Facts Label	\$0.143/kWh
Choose	ECONergy Energy Company, Inc. Tex Flex Plus Plan	\$158	3%	12		Terms of Service ; Facts Label	\$0.158/kWh
Choose	ECONergy Energy Company, Inc. Tex Flex Plan	\$158	3%	0		Terms of Service ; Facts Label	\$0.158/kWh
Choose	Reliant Energy Flex Plan	\$157	4%	0		Terms of Service ; Facts Label	\$0.157/kWh
Choose	Stream Energy Residential Service Two-Year Fixed Rate	\$146	10%	24		Terms of Service ; Facts Label	\$0.1455/kWh
Choose	Stream Energy Residential Service Three-Year Fixed Rate	\$146	10%	36		Terms of Service ; Facts Label	\$0.1455/kWh
Choose	Stream Energy Residential Service Month to Month	\$146	10%	1		Terms of Service ; Facts Label	\$0.1455/kWh
Choose	Stream Energy Residential Service One-Year Fixed Rate	\$146	10%	12		Terms of Service ; Facts Label	\$0.1455/kWh
Choose	Spark Energy, L.P. Spark Online Advantage 12	\$132	19%	12		Terms of Service ; Facts Label	\$0.132/kWh
Choose	National Power Company Heat Wave Plan	\$135	17%	12		Terms of Service ; Facts Label	\$0.135/kWh
Choose	National Power Co. Fast Track Savings Plan - Fixed Rate	\$141	13%	12		Terms of Service ; Facts Label	\$0.141/kWh
Choose	National Power Co. Power to Save Plan - Variable Rate	\$155	5%	0		Terms of Service ; Facts Label	\$0.1551/kWh
Choose	Reliant Energy Simple Solutions Renewable Plan	\$162	1%	0		Terms of Service ; Facts Label	\$0.162/kWh
Choose	Reliant Energy 2007 Secure Plan	\$154	7%	16		Terms of Service ; Facts Label	\$0.154/kWh
Choose	Green Mountain Energy Company Pollution Free	\$163	0%	0		Terms of Service ; Facts Label	\$0.1633/kWh
Choose	TXU Energy Price Guarantee 24sm	\$152	7%	24		Terms of Service ; Facts Label	\$0.152/kWh
Choose	TXU Energy Summer Savings 24sm	\$150	8%	24		Terms of Service ; Facts Label	\$0.15/kWh
Choose	TXU Energy Price Guarantee 12sm	\$154	6%	12		Terms of Service ; Facts Label	\$0.154/kWh
Choose	TXU Energy Freedom Plan	\$155	5%	1		Terms of Service ; Facts Label	\$0.155/kWh

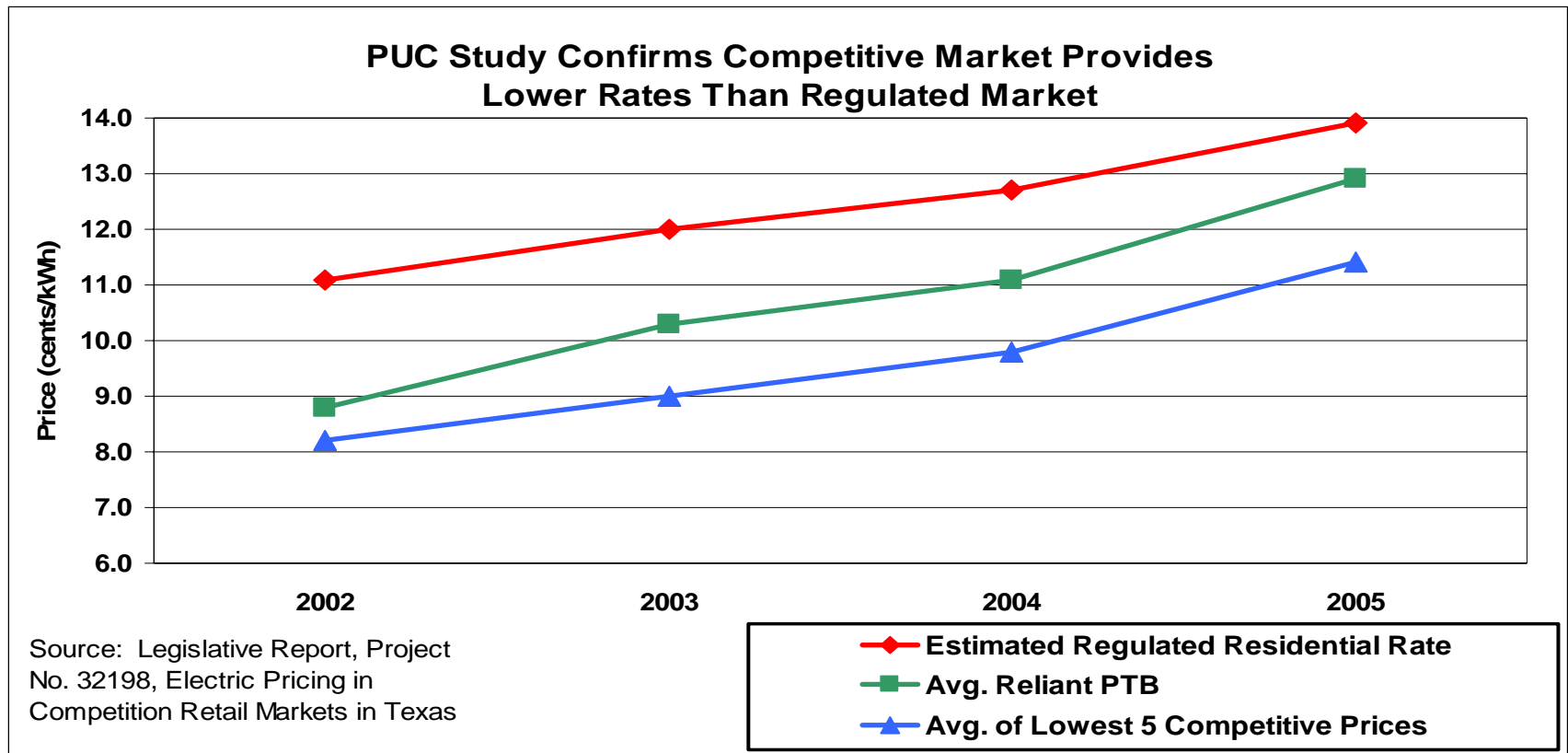
Competitive Offers in Texas (continued)

Choose	Reliant Energy Price to Beat	\$163	0%	1		Terms of Service ; Facts Label	\$0.163/kWh
Choose	Green Mountain Energy Co. Pollution Free-Reliable Rate	\$160	2%	12		Terms of Service ; Facts Label	\$0.16/kWh
Choose	Texas Power Texas Power Plan	\$144	12%	1		Terms of Service ; Facts Label	\$0.144/kWh
Choose	Direct Energy, LP Price Protection Plan	\$151	7%	12		Terms of Service ; Facts Label	\$0.151/kWh
Choose	StarTex Power Star Seasonal Savings Month to Month Plan	\$135	17%	1		Terms of Service ; Facts Label	\$0.135/kWh
Choose	StarTex Power Star Seasonal Savings 1 Year Plan	\$139	15%	12		Terms of Service ; Facts Label	\$0.139/kWh
Choose	StarTex Power Star Seasonal Savings 2 Year Plan	\$142	13%	24		Terms of Service ; Facts Label	\$0.142/kWh
Choose	StarTex Power Star Seasonal Savings 3 Year Plan	\$141	13%	36		Terms of Service ; Facts Label	\$0.141/kWh
Choose	StarTex Power Super 6 Star Savings 6 Month Plan	\$129	21%	6		Terms of Service ; Facts Label	\$0.129/kWh
Choose	StarTex Power StarSavings 1 Year Plan	\$150	8%	12		Terms of Service ; Facts Label	\$0.15/kWh
Choose	StarTex Power StarSavings 2 Year Plan	\$147	10%	24		Terms of Service ; Facts Label	\$0.147/kWh
Choose	StarTex Power StarSavings 3 Year Plan	\$144	12%	36		Terms of Service ; Facts Label	\$0.144/kWh
Choose	StarTex Power StarSavings Month to Month Plan	\$148	9%	1		Terms of Service ; Facts Label	\$0.148/kWh
Choose	Cirro Energy Residential Electric Service	\$144	12%	12		Terms of Service ; Facts Label	\$0.144/kWh
Choose	Dynowatt Residential Service	\$138	15%	1		Terms of Service ; Facts Label	\$0.138/kWh

43 Offers* – as much as 22% discount off the standard offer!

* Not all offers are listed on www.powertochoose.org . Listing of offers by retailers is purely voluntary.

In TX, Choice has Occurred With Prices Lower Than What Would Have Occurred Under Regulation



PUC study data shows almost \$3 billion in value to residential customers





Current Default Structure Will Not Encourage Efficient Consumption and/or Investment Decisions

- Market responsive default structure leads to knowledge of price signals
- This knowledge leads to choice and action, and will yield meaningful load reduction, more efficient utilization of generation assets, peak clipping, and system-wide cost reduction
- Center for Energy, Economic & Environmental Policy at Rutgers University, *Assessment of Customer Response to Real Time Pricing and Assessment of Customer Response to Real Time Pricing, Task 2: Wholesale Market Modeling of New Jersey and PJM*

Retailers Desire to Enter the Illinois Market

- Why?
 - Contributes to business model
 - Growth opportunity
 - Improves economies of scale
- However, because current structure is a barrier to sustainable competition, retailers – employing prudent business decision criteria – will not enter this market

Recommended Default Service Features for a Successful Market Structure

Design Features	Market Responsive Model	Long-Term Procurement Model	Rate Capped Model
Provides customers reasonable price protection while allowing ongoing opportunities for an ARES to participate in the market		X	X
No switching restrictions to impede customer choice		?	?
Default pricing that is responsive to market forces		X	X
Vigorous customer choice/competition		X	X

Recommended Elements of a Market Responsive Default Structure

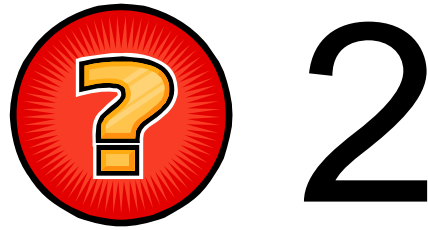
- The Default product should be fairly priced including consideration of the risks of providing service (e.g. switching)
- The Default product should be a basic service and not interfere with products that could be offered by the competitive market (e.g. long-term, fixed price product)
- The Default product resulting from a wholesale auctions should be sufficiently adjusted to reflect changes in the market (e.g., 12 annual adjustments)
- Experience shows that there are no long-term default service designs that result in meaningful customer choice or consumer-oriented benefits
- Default provider should be free to procure supply in a manner that best meets the providers risk profile – e.g. the method of supply procurement should not be mandated

Conclusions

- Default designs that use non-market responsive, long-term contracts will not produce sustainable competition, and will not provide the benefits of choice, innovation and efficiencies
- The benefits to consumers resulting from competition are real
- Moving to a market-responsive default structure will allow for competition, produce consumer benefits, produce environmental benefits and lead to system-wide efficiencies

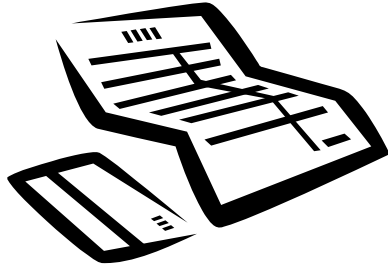
Next Steps

- Carefully consider changes in the default structure in the next procurement cycle
- Next opportunity: December, 2006

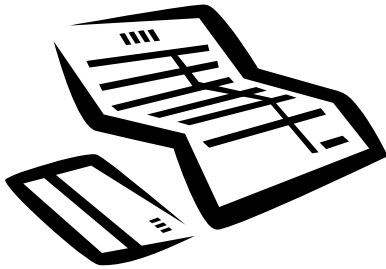


Will we have to create a new billing system or can we pay the utility to bill for us?

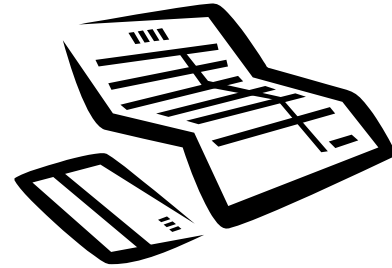
Utility Consolidated Billing



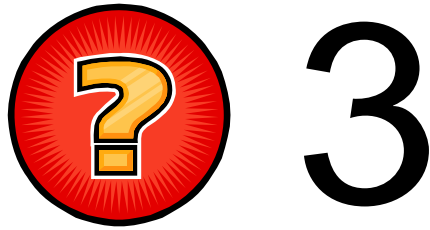
Utility Bill



ARES Bill



ARES Charges
Included
On Utility Bill



Will we be on equal footing
with utility default service in
terms of uncollectible
expense?

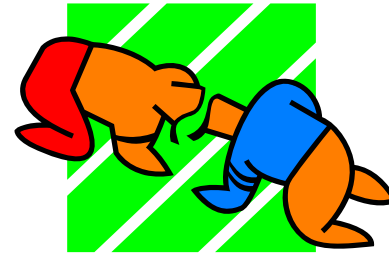
State regulation essentially guarantees utilities recovery of their receivables.

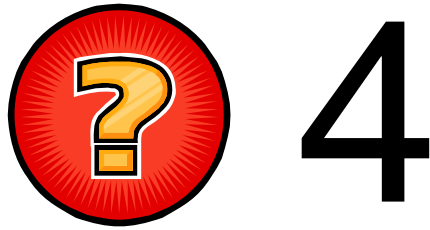


In states without purchase of receivables programs, marketers have no equivalent guarantees that they will recover their receivables.



Purchase of
receivables
programs assure
that marketers'
energy products will
be on equal footing
with utility default
service in terms of
uncollectible
expenses.





Is the process for switching energy providers simple, straightforward and efficient?

Customer Switching Process

- **Issues:**

- Customer Sign-up Channels are limited
- Manual and Costly Enrollment Processes
- Unnecessary Rework on Customer Information

- **Importance:**

- Choice Enrollment has to be Simple, Straightforward, Efficient and Positive Experience for the Customer. For the Supplier, it needs to be Efficient.

- **Suggested Improvements:**

- Allow Sign-ups thru Various Channels (e.g. Multiple Ways to Sign-up Customers: Reply Cards, Internet, Inbound and Outbound Telephonic with Recorded Affirmations)
- Require the Utilities to Provide Customer Lists with a Sign-up Identifier
- Streamline Manual Enrollment Processes/Rework

Ways to Stimulate Customer Switching

- **Issues:**

- Low Involvement Decision for the Customer
- Customers Will Not Choose Unless They Understand the Program and Feel Comfortable That They will Receive a Benefit
- Need to Implement Programs the Get the Choice Engine Working

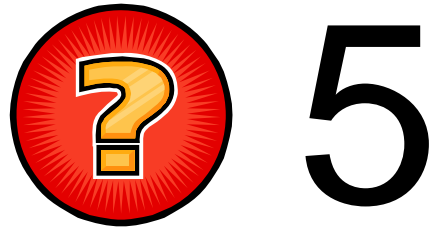
- **Importance:**

- Greater Customer Participation creates a More Robust, Efficient, and Competitive Retail Market
- True Competitive Market will Manage Prices, Force Creativity, and Improve Supply Procurement Efficiency

Ways to Stimulate Customer Switching

- **Suggested Retail Choice Programs:**

- Utility Programs that Encourage New/Existing Customers to Consider Their Options (Benefit: Utilities Showing Active Support of Choice Programs helps in Customer Involvement)
- Utility Referrals Programs (NY, CT) (Benefit: Get a Significant Share of Customers Participating in Choice and They Receive Short Term Savings)
- Special Utility/Customer Incentives for Switching (NY) (Benefit: Customer One Time Incentive to Participate)
- Voluntary Retail Allocation Programs (Dayton Power & Light, Virginia Power) (Benefit: Guaranteed Savings for One/Two Period; Gets Interested Customers Involved)
- Market Share Retail Allocation Programs (PECO) (Benefit:Guaranteed Savings and Participation)



Is there an active and ongoing effort by regulators and other policy makers to foster the development of retail competition in the market?

Competitive retail electric markets require ongoing and active involvement of regulators and policymakers.



Suggested Next Steps

Determine the role of utility default service in the transition to competitive retail electric markets.

- Decide issue in upcoming formal review of the auction process.

Encourage ComEd and Ameren to develop Utility Consolidated Billing and Purchase of Receivables Programs.

- Seek legislation to give ICC authority to mandate UCB / POR programs

Champion ways to make switching providers simple, straightforward and efficient.

- Seek legislation to authorize telephonic enrollment.
- Develop a statewide policy position on ARES referral programs

Secure additional Staff resources to work on retail electric competition issues.

- Encourage passage of HB 4977.

Closing Thoughts

Marketers want to provide consumers with alternatives to ComEd and Ameren's rates.

The environment for residential retail competition in Illinois needs improvement.

The steps we have outlined today will go a long way toward attracting marketers to Illinois.